

# **SALES AND USE TAX REVIEW COMMISSION**

## **RECOMMENDATION PURSUANT TO P.L. 1999, C. 416**

**BILL NUMBER: S-1652**

**DATE OF  
INTRODUCTION: 9/25/00**

**SPONSOR: Senator Turner**

**DATE OF  
RECOMMENDATION: 12/22/00**

**IDENTICAL BILL:**

**COMMITTEE: Senate Community and Urban Affairs (SCU)**

### **DESCRIPTION:**

This bill would create “Urban Heritage Districts.” These small districts would be located within municipalities qualified to receive urban aid, and would contain historic sites and meet certain other requirements.

Vendors having a place of business within designated “urban heritage districts” would be eligible to charge sales tax at one-half the normal rate on retail sales made from their urban heritage district location (except sales of motor vehicles, cigarettes, alcoholic beverages, and manufacturing machinery, and except when the business is located in an area that overlaps with an urban enterprise zone.) The Division of Taxation would be required to certify those vendors eligible to charge the reduced sales tax rate as urban heritage district vendors.

Sales tax revenues from the reduced-rate retail sales made by certified urban heritage district vendors would be deposited into an Urban Heritage District Maintenance Trust Fund.

**ANALYSIS:**

This bill would result in many of the same undesirable conditions already caused by the urban enterprise zone reduced sales tax rate benefit program. Even assuming that the reduced sales tax rate benefit might attract new business to the urban heritage districts favored under the terms of the bill, the piecemeal creation of such specially favored districts will simply shift economic growth from one neighborhood to another; if an “urban heritage district” does experience an increase in healthy economic activity, its good fortune would be at the expense of neighboring districts, which arguably, would be placed at a competitive disadvantage in attracting new vendors or customers willing to engage in transactions at the full 6% rate.

A special reduced sales tax rate for sales within certain portions of New Jersey will also create a potential legal problem, if the full compensating use tax rate is applied when taxable tangible personal property purchased out-of-state or from non-New Jersey mail order vendors is “used” in an urban heritage district. By the terms of the bill, the one-half reduced sales tax rate would apply only to sales made from a certified vendor at its place of business in an urban heritage district. But giving full effect to this physical-location requirement could result in a violation of the Commerce Clause of the United States Constitution. The state cannot lawfully subject a sale of merchandise taking place within New Jersey to only 3% sales tax, while imposing a use tax rate of 6% on a comparable item that was purchased from an out-of-New Jersey source.

In Associated Industries of Missouri v. Lohman, 511 U.S. 641, 114 S. Ct. 1815, 128 L. Ed. 2d 639 (1994), the United States Supreme Court held that Missouri’s sales and use tax scheme violated the Commerce Clause in any localities where the state use tax exceeded the local sales tax. The tax scheme at issue in the Associated Industries case contained several layers. The statutes and constitution of Missouri imposed various state sales taxes, and, in addition, state legislation authorized political subdivisions to enact their own local sales taxes. Many localities did so. Thus, in some localities, the combined use tax was lower than the combined sales tax rate, while in others, the use tax was higher. The Court considered it irrelevant that the tax scheme lacked any discriminatory intent. Instead, it concluded that the test for validity of a compensatory use tax required mathematical precision: in order to be permissible under the Commerce Clause, any use tax rate imposed on an item purchased out-of-state had to be no more than the sales tax rate imposed on a similar transaction within the state. It therefore held that the effect of Missouri’s tax scheme impermissibly discriminated against interstate commerce in any locality where the sales tax rate was less than the use tax rate.

In light of the Associated Industries ruling, it appears that New Jersey statutes creating a partial exemption for certain retail sales only if they take place within a certain district (i.e. only intrastate sales) would similarly not survive constitution scrutiny. In order to avoid constitutional challenges, New Jersey has had to apply the reduced (3%) rate administratively both to sales actually taking place in UEZ or Salem County and satisfying the other statutory criteria for the partial exemption and to any out-of-state purchases, when the first use of the goods takes place in Salem County or a UEZ. If this bill is enacted, it will need to do the same thing for use tax in the urban heritage districts. Only in that way could the partial exemption not discriminate against interstate commerce, since both sales tax and use tax would be 3%. But, while this solution would at least probably shield the State from constitutional attacks, it would result in substantial losses in tax revenue and would fail to advance the purpose for which the urban heritage district partial exemption is intended.

**RECOMMENDATION:**

The Commission does not recommend enactment of this bill.

**COMMISSION MEMBERS FOR PROPOSAL:**

**COMMISSION MEMBERS AGAINST PROPOSAL: 7**

**COMMISSION MEMBERS ABSTAINING:**

**COMMISSION MEETING DATE: 11/28/00**